

structures pressures ILECs to use a uniform rate structure that may not match the cost characteristics of a specific ILEC or meet market needs.

The Commission has only addressed a small part of this problem in its Third Report and Order. The majority of new switched access rate structures will, in fact, be needed to respond to growing competition, and the Commission has offered no relief for these important structure changes. With the rule changes of the Third Report and Order, SNET and other ILECs will be required to meet a public interest standard to meet Part 69 rule requirements. Even this new process will delay SNET's introduction of new services to its customers, a delay that SNET's competitors do not face.

It took over a year to be granted a Part 69 expedited waiver request for SNET elements. SNET's Petition for Waiver had only sought to extend the same structure in place for special access services to switched services, and was not opposed.

A new, streamlined approach to Part 69 is needed. The new procedure should apply to all switched access plans, including those that meet competitive customer needs.

In the alternative, and to speed the introduction of new services, ILECs should be allowed to file a waiver concurrently with a proposed tariff. The inclusion of added tariff detail at the ILEC's option would aid customers and the Commission in evaluating the merits of the waiver request.

**Phase 2:**

ILECs should be granted this next phase of deregulation when there is a demonstration of actual competition in the state. Services should be removed from price cap regulation in this step. The transition to Phase 2 deregulation should be allowed to occur in geographic areas smaller than a state. ILECs should be required to show key indicators that indicate actual competition, such as 1) state approval of interconnection agreements with one or more competitors, 2) the number of unbundled loops, and resale services in place, 3) the number of NXX codes assigned to competitive local exchange carriers, 4) the number of minutes of use being exchanged with competitors, 5) a listing of services offered by competitors, and 6) geographic description of the geographic area served by competitors.

**Forbearance:**

Forbearance from regulation of a service should occur when the three pronged test of Section 10(a) of the Act is met. Enforcement is not necessary to ensure that access rates are just and reasonable or not unjustly or unreasonably discriminatory, enforcement is not necessary for the protection of consumers, and forbearance is consistent with the public interest.

Regulation should be eliminated in markets where competitive forces effectively constrain prices for products in a geographic area.

B. Immediate Forbearance From Regulation For Certain Services Would Be Appropriate.

Sufficient evidence exists to support forbearance from regulation of special access services. Given the active presence of competitive providers of dedicated facilities and the existence of collocation arrangements, this same forbearance should also extend to switched access entrance facilities and direct trunked transport services. Switched access entrance facilities and direct trunked transport are special access, and should have the same regulatory treatment.

There have been direct substitutes for special access services in the marketplace for years. Displacement of special access requires no interconnection with ILEC switches, hence special access is especially attractive to ILEC competitors as it contains no "bottleneck." As USTA points out in its comments, regulation is unnecessary to ensure that special access and direct trunked transport services are not unreasonably discriminatory and regulatory enforcement is not necessary for the protection of consumers.

SNET recommends that Directory Assistance service (DA) be forborne from regulation as well. USTA explains that for all ILECs, directory assistance is highly competitive. Competition for DA is robust in Connecticut, and SNET needs to meet market rates for these services. DA, and indeed all forms of operator services, are now current offerings of all the major IXC's -- AT&T, MCI, Sprint, LDDS/Metromedia -- as well as other non-traditional carriers who have entered the market. Since July of

1993, over 100 non-facilities-based, switched resellers have applied for certificates of public convenience and necessity in Connecticut, and 39 of those companies have indicated an interest in providing Operator Services. Competitive local service providers in Connecticut can choose to route their DA traffic to such providers as Excell Agent Services, InFo NXX, Clifton Forge, Teletrust, and Frontier just to name a few.

Large businesses are actively purchasing Connecticut listings from other providers at lower rates. Some Connecticut businesses plan to use MetroMail, a National Directory Assistance database provider, by accessing their data bases directly. Additionally, SNET is losing customers who are using the Internet as well as various CD-ROM applications that are available in the market place today. The largest losses, however, may result from AT&T routing traffic to its own operator services platform.

In sum, competition for Directory Assistance is a reality in Connecticut. DA, and indeed all operator services, should be removed from regulation now.

C. A Prescriptive Approach To Access Reform Is Unnecessary.

The Commission's prescriptive approach to access reform will not foster the rapid development of competition in the access market. To the contrary, a

prescriptive approach is actually regressive, especially in Connecticut.<sup>19</sup> The prescriptive approach substitutes regulation for competition and assumes that regulators can know and/or control the development of competitive alternatives by access providers other than ILECs. This of course is not possible. The prescriptive approach is "policy-based" and therefore by definition inconsistent with a competitive market.

D. Neither TSLRIC Nor TELRIC Is Appropriate For Pricing Access.

The Commission tentatively concludes that the goal for prescriptive access reform should focus on interstate access rates based on some form of a TSLRIC pricing method.<sup>20</sup> The Commission also seeks comment on whether there is a generic cost model that could be used to determine TSLRIC-based interstate access prices.<sup>21</sup> It is not appropriate to require ILECs to use any specific or prescribed proxy cost model to determine interstate access prices. As has been demonstrated in the proceedings associated with the universal service fund, there is widespread disagreement about the validity of proxy cost models and the accuracy of their output

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<sup>19</sup> See "Connecticut Has Been Progressive In Fostering Competition," pg. 12, above. Also, as Chairman Hundt has aptly noted: "The less a state does to create the conditions for local competition, the stronger the argument for the FCC to take a prescriptive approach instead of a passive approach to interstate access in that market." Remarks of FCC Chairman Hundt before the Competition Policy Institute, January 14, 1997, pg. 2 at para. 4).

<sup>20</sup> NPRM, para. 222.

<sup>21</sup> NPRM, para. 226.

results. Proxy models clearly do not, and cannot, capture unique aspects of specific geographic and technological applications.

In particular, with respect to the Commission's inquiry into the feasibility of TELRIC in deriving the costs of access service,<sup>22</sup> SNET asserts that TELRIC is not an appropriate method for this purpose. TELRIC does not provide any recovery of embedded or historical costs (prudent costs which ILECs incurred under a regulatory obligation to construct and operate a ubiquitous network as the supplier of last resort), and assumes using the most efficient telecommunications technology currently available, regardless of the technology actually employed by the ILEC. TELRIC thereby underestimates ILEC costs and results in prices that are too low, effectively requiring that ILECs subsidize their competitors, and threatening the viability of the ILEC business. Therefore, TELRIC cannot be even remotely considered "competitively neutral."<sup>23</sup>

E. No Change To The Current The Cost Of Capital Is Necessary.

The Commission invites discussion on alternative prescriptive methods to reduce access rates by applying a lower rate of return target.<sup>24</sup> SNET recommends

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<sup>23</sup> Indeed, it is simply not true that "no one disputes that TELRIC is competitively neutral." (Speech of Chairman Reed Hundt before the Competition Policy Institute, January 14, 1997, page 2.) ILECs and others have long maintained that TELRIC produces costs and rates that are artificially low, and that this outcome is certainly not competitively neutral. See generally Iowa Utilities Board et al. v. FCC, No. 96-3321 and consolidated cases (8th Cir. Oct. 15, 1996), *partial stay lifted in part*, Iowa Utilities Board et al. v. FCC, No. 96-3321 and consolidated cases (8th Cir. Nov. 1, 1996).

<sup>24</sup> NPRM, para. 228.

that the Commission not prescribe access rate reductions. SNET disagrees with any prescriptive method that would simply drive access rates down. The market is driving access rates to economic levels.

Business risks for the ILECs are increasing, not decreasing, and are causing the cost of capital to rise. In the face of increasing business risk such as loss of customers because of competition, investors are demanding higher returns as compensation for this higher risk. Other uncertainties (for example, those associated with current legal and regulatory proceedings, and the eventual entry of the RBOCs into long distance) are also increasing the perceived risks of local exchange carriers, especially smaller ones like SNET.

In sum, the allowed cost of capital should not be changed as a way of reinitializing access rates.

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IV. A LIMITED PRESCRIPTIVE APPROACH COULD BE USED DURING A SHORT TRANSITION PERIOD. (NPRM, paras. 218-233.)

Rather than rely on a prescriptive approach to access reform, SNET continues to recommend that the Commission would better serve consumers by implementing a market-based approach. Access is a commodity product, and so regulation of access -- whether by price regulation, rate of return or other system -- interferes with the operation of the market, and with consumer decisions on products and pricing.

As an alternative to permitting the market to set prices, the Commission proposes a policy-based mechanism where a prescriptive approach would produce rate decreases. Yet the Commission itself prefaces this proceeding by recognizing that current rates, based on prescriptive Part 69 rules, "are fundamentally inconsistent with the competitive market conditions that the 1996 Act attempts to create."<sup>25</sup>

While SNET believes that a market-based approach to access reform is required in the current competitive environment, a brief transition to that approach could be accomplished with minor revisions to the price cap plan.<sup>26</sup> Even so, SNET urges that the Commission observe caution in making these revisions. An overly-

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<sup>25</sup> NPRM, para. 6.

<sup>26</sup> In response to the Commission's invitation (NPRM, at note 223), and in order to provide the Commission with additional information in this proceeding regarding the need for price cap rule changes, SNET attaches here as Exhibit 3 SNET's Pricing Flexibility Comments filed December 11, 1995 in CC Docket No. 94-1, Price Cap Performance Review for Local Exchange Carriers.



prescriptive approach will not stimulate new competitive entrants into the access market. The Commission can stimulate new entrants and a robust market by moving the LECs' access offerings to a cost-causative regime, and letting the LECs sink or swim as a result of their cost-causative pricing and their delivery of service.

A. An Increase In The Price Cap X-Factor In This Competitive Access Environment Is Not Warranted. (NPRM, paras. 231-235.)

As part of its prescriptive alternative to access reform, the Commission proposes that the productivity offset X-Factor used in the price cap formula be increased as a way to effect reductions in access rates.<sup>27</sup> SNET avers that a mandated upward adjustment in its X-Factor is not warranted, given SNET's experience. An upward adjustment would be contrary to the pro-competitive thrust of the Act, as well as the Commission's own objectives. Simply stated, forced reductions in LEC access rates will not produce a more competitive interstate access market.

A review of SNET's experience since electing price cap regulation demonstrates just how unfounded and detrimental an increase in the X-Factor would be to SNET. SNET has never been able to chose an X-Factor in the earnings sharing range, nor has it ever earned in the sharing range.<sup>28</sup> To assume now that

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<sup>27</sup> NPRM, paras. 231-235.

<sup>28</sup> See SNET Forms 492A, 1991-1996 Annual Access Tariff Filings.

SNET's earnings are as high as other ILECs, overlooks the real heterogeneity in the industry.<sup>29</sup> Treating all price cap ILECs the same would disregard fundamental differences in the scale and scope between service providers, as well as the regional economics between the small and mid-sized elective price cap ILECs, and the high earning RBOCs and GTE. SNET is a single state ILEC and is not able to benefit from geographic and regional diversification enjoyed by the RBOCs and GTE. SNET cannot offset the prevalent lackluster economic situation in Connecticut with strong growth in other markets. The Commission's selection of the appropriate level for the X-Factor must not assume that "one-size-fits-all."

SNET entered price caps with an understanding that the Commission promised a price cap plan where there was "a corresponding need to provide the ILECs with reasonable yet challenging productivity alternatives."<sup>30</sup> In fact, the productivity options available to SNET have been so challenging that SNET has never been able to achieve earnings in the sharing range. These results demonstrate the Commission's correct understanding that small and mid-sized companies "may have fewer opportunities than large companies to achieve cost savings and efficiencies."<sup>31</sup> As the Act encourages efficient pricing and market-

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<sup>29</sup> In the Matter of Price Cap Performance Review for Local Exchange Carriers, CC Docket No. 94-1, First Price Cap Report and Order, released April 7, 1995 (FCC 95-132), para. 165.

<sup>30</sup> Ibid.

<sup>31</sup> In the Matter of Policy and Rules Concerning Rates for Dominant Carriers, CC Docket No. 87-313, Second Report and Order, released October 4, 1990 (FCC 90-314), para. 103.

based outcomes, simply adopting a higher X-Factor, as suggested by AT&T and MCI,<sup>32</sup> would not be appropriate.

In sum, an X-Factor increase would not be an appropriate transition mechanism toward access reform.

B. The X-Factor For The Transition Period Should Be Based Upon Total Factor Productivity. (NPRM, para. 233.)

SNET joins USTA in recommending an X-Factor based on total factor productivity (TFP) for the transition period.<sup>33</sup> This recommendation is consistent with the Commission's treatment of AT&T during its transition to non-dominant status. The Act contemplates that competition will dilute different services at a different pace in different areas throughout the country.

The ILEC industry will access customers to interconnectors, who will substitute their negotiated interconnection agreements for ILEC tariffed access services.<sup>34</sup> ILECs, particularly small and mid-sized companies, will lose access revenues faster than they can shed access costs. As a result, the productivity of these small and mid-sized price cap carriers is in particular jeopardy.

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<sup>32</sup> NPRM, para. 233.

<sup>33</sup> See Comments of USTA filed today in these proceedings, Sect. I. C.

<sup>34</sup> Some sources informally predict that the LECs will be non-dominant within three years, and will lose over 30% of their market share.

SNET concludes that the Commission can best implement a transition to market-based pricing by adopting a TFP-based X-Factor. This approach is harmonious with the Commission's goal to replicate the incentives created by competition,<sup>35</sup> leaves all elements of the price cap formula intact, and is the logical and sustainable way for the Commission to proceed.

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<sup>35</sup> In the Matter of Local Exchange Carrier Performance Review, CC Docket No. 94-1, Fourth Further Notice of Proposed Rulemaking, released September 27, 1995 (FCC 95-406) para. 108.

V. THE ACCESS RATE STRUCTURE SHOULD BE MODIFIED TO REFLECT COST-CAUSATION.

A. Common Line (NPRM, paras. 57-70.)

1. The Carrier Common Line Portion Of Subscriber Loop Costs Should Be Assessed IXCs Based Upon PICs.  
(NPRM, para. 60.)

The Commission seeks comment on alternate methods of recovering the CCL portion of Subscriber Loop Costs, including the following:

1. Flat per Line charge - assessed to IXCs based on the end user's PIC;<sup>36</sup>
2. CPI's proposal for "bulk billing" to IXCs based on percent share of interstate MOU or revenues;<sup>37</sup>
3. "Capacity Charge" assessed to IXCs based upon the number and type of trunks that they purchase from ILECs; or a "trunk port charge" to each IXC based on the number of trunk-side ports; or a "trunk port and line port" charge based on the number of trunk-side ports and line-side ports.<sup>38</sup>

SNET prefers Option #1. CCL costs are related to the costs of the loop, caused by the provision of a connection to the end user.<sup>39</sup> As these costs are not

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<sup>36</sup> NPRM, para. 60.

<sup>37</sup> NPRM, para. 61.

<sup>38</sup> NPRM, para. 61.

<sup>39</sup> SNET states that the Commission, and indeed the Joint Board, must eventually do the right thing and allow full cost recovery from the end user, perhaps on a deaveraged basis, of the full cost of the local loop common line connection. To postpone doing otherwise simply delays the benefits of competition, requires other consumers to pay for end user costs, and potentially prevents LECs from recovering their prudently incurred costs.

related in any way to the amount of interexchange originating or terminating traffic (such as number of calls or the length of time for those calls) carried over that loop, these costs should ideally be recovered from the end user directly. Ideally, these costs should be included as part of the end user's local exchange rate.

Option #1 has the greatest advantage of being the simplest to apply and the least costly to administer. Common line cost assessment to IXC's based on the number of presubscribed lines (as compared to traffic or revenue quantities) is cost-causative. Any concerns about end users deliberately not selecting a PIC to avoid the SLC can be avoided by allowing the ILEC to bill end users directly. IXC's serving end users who bypass their network via "dial-around" access or who make few or no toll calls may continue to be disadvantaged in the marketplace, but this is not a new problem, nor one which should be solved by a less cost-causative assessment of end user loop expenses. To ensure recovery of their costs, IXC's are free to establish their own flat monthly charges to presubscribed end users or reassess their own marketing strategies.

In sum, SNET agrees with USTA that CCL should be billed on a "per-line" basis, instead of the current "per-minute-of-use" charge paid by the IXC's.

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2. One SLC Should Apply Per ISDN Service.  
(NPRM, para. 68.)

The Commission requests comment on the number of SLCs that should be applied to derived channels, such as ISDN services.<sup>40</sup> SNET strongly believes that the application of one SLC or End User Common Line (EUCL) charge per ISDN channel or service is appropriate. Application of end user charges should be "technology-neutral," minimizing adverse rate impacts for customers seeking new, advanced technologies. ISDN service, as an example of a new technology offered by ILECs, should not be unfairly burdened with paying more than one end user charge. This is especially true when the underlying costs studies support the application of a single charge.

SNET agrees that if non-traffic sensitive costs of ISDN service (Basic Rate Interface (BRI)) approximate the non-traffic costs of ordinary loops, a single end user charge should also apply to ISDN service.<sup>41</sup> Like other ILECs, SNET's demand for its primary rate interface (PRI) service is very small, compared to the demand for its BRI service. SNET does not recommend a different application of end user charges for this ISDN service.

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<sup>40</sup> NPRM, paras. 68-70.

<sup>41</sup> GTE Comments filed October 30, 1995, pgs. 8-10 (calculating Bell Atlantic's ratio at 1.0, Pacific Bell's at 1.03, NYNEX's at 1.0 and Ameritech's at 1.07).

In sum, SNET recommends that it continue to charge one end user charge for ISDN service.

3. The SLC Should Not Be Different For Additional Residential Lines. (NPRM, para. 65.)

The Commission proposed to increase the cap for SLC on second and additional lines for residential customers.<sup>42</sup> While this would be an additional source of revenue, the administrative burdens associated with identification of these lines so that they could be billed the higher SLC, would outweigh this benefit. SNET presently has no systems in place that would identify these lines. In addition, when there are alternative local providers, a customer could have two lines, one from each provider. It would be almost impossible to determine which line was the second line in order to apply the higher SLC.

4. SLCs For Multi-Line Businesses Could Be Increased To Compensatory Levels. (NPRM, para. 65.)

The Commission proposes to increase the cap on the SLC for multi-line businesses to the per-line costs assigned to the interstate jurisdiction.<sup>43</sup> SNET does not object to this proposal, and supports it for those ILECs whose per-line cost is

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<sup>42</sup> NPRM, para. 65.

<sup>43</sup> NPRM, para. 65.



above the cap.<sup>44</sup> It makes solid economic sense for the Commission to move toward cost-causation in its access reform regime by increasing the business SLC cap to cost.

5. Subscriber Line Charges Should Be Deaveraged.  
(NPRM, para. 67.)

The Commission asks whether it should permit or require ILECs to deaverage SLCs geographically.<sup>45</sup> SNET strongly supports geographic SLC deaveraging as a way for the Commission to move swiftly into cost-causation, and to respond to the cost characteristics of the ILECs. SNET's competitors provide services in areas which are less costly to serve. Customers in less costly areas should be able to take advantage of offerings that reflect those costs. Deaveraged SLCs on a geographic basis provides ILECs with a opportunity to be more responsive in the marketplace, a goal fostered by the Act and the Commission.

B. Local Switching (NPRM, paras. 71-79.)

The Commission proposes to establish a flat charge to recover the portion of local switching costs that are NTS; the Commission seeks comment on whether all shared local switching charges are driven by the number of lines and trunks.<sup>46</sup>

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<sup>44</sup> This is not the case for SNET, as its interstate cost, and its rate for the interstate portion of the business local loop, is \$5.99 per month.

<sup>45</sup> NPRM, paras. 67, 180.

<sup>46</sup> NPRM, para. 72-73.

Network technologies, associated cost-drivers and market demands have changed significantly since 1984 and will continue to do so. Although the Commission has put forth some logical proposals for Local Switching and other switched access rates, there is no need for the Commission to codify any type of rate structure. These decisions should be left to ILECs and their customers.

There is no real disagreement that the components of access are essentially identical to other forms of switched interconnection. ILECs are already bound by the Act, the Commission's Interconnection Order, state rulings and negotiated agreements to establish cost-causative rates for unbundled network components. Rate structures for unbundled components and access services will naturally converge since one can be used as a substitute for the other. Continuing separate rate structures is in no one's interest and will increase costs to both the supplier and customers.

IXCs and other access customers clearly have expressed a need for national standardized rate structures. Without a large degree of standardization, IXCs would face large increases in administrative costs as they tried to order access facilities and verify bills. It is not necessary, however, for the Commission to play this management role. If SNET is to continue doing business with its large customers, it will simply have to comply with their needs, or they will go elsewhere.

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C. Transport (NPRM, paras. 80-95.)

The Commission tentatively concludes that Entrance Facilities & Direct-Trunked Transport rate structures should mandate flat-rated charges, and inquires whether ILECs should be permitted to offer facilities based on whether the ILEC or IXC is responsible for channel facility assignments.<sup>47</sup>

ILECs should be able to eliminate the interim transport rate structure's mandated option of usage-sensitive charges on flat-rated facilities. SNET supports the Commission's tentative conclusion to allow ILECs to assess a more cost-causative flat-rate charge for dedicated transport services. Since some ILECs may wish to continue to offer usage-based alternatives, there is no need to require ILECs to assess only flat-rates charges.

Even if the Commission doesn't eliminate Part 69 rules on other categories, it should recognize that the provision of transport facilities is the most competitive aspect of access, and therefore it should remove all remaining rate structure constraints on these services.

ILECs should have the opportunity to charge flat rates for dedicated facilities that are not usage-based in their costs, and retain the option to charge customers on a different basis if that is mutually agreeable.

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<sup>47</sup> NPRM, para. 86.

D. Transport Interconnection Charge (NPRM, paras. 96-122.)

The Commission's investigation into the usage-rated transport interconnection charge (TIC) is a significant part of its access reform investigation; it proposes a mechanism to phase out TIC "in a manner that fosters competition and responds to the court's remand."<sup>48</sup>

The regulatory history of the TIC dictates that reform of this access element is an absolute necessity. The Commission now has an opportunity to allow recovery in accordance with cost-causation principles.

SNET also recognizes the complexity and difficulty of this task, due to the allocation rules in Parts 36 and 69 and the pricing and subsidy policies embodied in those rules. USTA has undertaken an analysis of the TIC, and is presenting in its Comments filed in this proceeding today the results of that investigation. ILECs should be provided the opportunity to recover of the TIC amount in full. SNET supports the analysis USTA has conducted and its recommendation for recovery of the TIC.<sup>49</sup>

In sum, the portions of the TIC that are identifiable service-related costs of trunking, transport and tandem switching should be moved to the appropriate elements for revenue recovery. The remainder of the TIC must continue to be

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<sup>48</sup> NPRM, para. 98.

<sup>49</sup> See Comments of USTA, Sect. III. D, and related attachments.

recovered and bulk billed to IXCs based upon their annual interstate retail or access revenues, pending a Commission proceeding to examine its separations rules.

E. SS7 Signaling (NPRM, paras. 123-138.)

SNET generally agrees with the Ameritech model for a revised SS7 rate structure for the industry.<sup>50</sup> However, the underlying technology necessary to implement the Ameritech model is not yet ready for commercial deployment. Considering the sizable investments required to implement the model, SNET is at this time reluctant to fully subscribe to the concept of unbundled SS7 elements.

The Commission should not mandate any rate structure for this type of equipment. In SNET's case, we are still in the preliminary phases of this issue, and are presently evaluating possible alternatives. Without knowing the potential costs of available alternatives, we reserve comment on possible rate structures or levels.

F. New Technologies (NPRM, para. 139.)

The Commission seeks comment on whether and how it should take new technologies into account in adopting access charge rules.<sup>51</sup> Commission policies regarding new technology should seek to achieve three primary objectives:

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<sup>50</sup> NPRM, para. 127.

<sup>51</sup> NPRM, para. 139.

1. Encourage new investments in technology by all competitors, including new market entrants and incumbent ILECs;
2. Encourage development of technically advanced products and services that meet emerging market needs, e.g., broadband data transport;
3. Encourage development of products and services that address current and future market issues, e.g., Internet access.

In general, service providers evaluate potential deployment of new technologies in a competitive environment in order to either 1) reduce cost of service, and/or 2) meet market needs. In either situation, every potential service provider, including new entrants and incumbents, attempts to differentiate themselves in the market, where features, functions and prices are the determining factors of success.<sup>52</sup>

New technologies should not be burdened with complying with traditional access charge rules and regulations, but should be managed by an enlightened Commission policy that emulates, to the greatest degree possible, competitive market forces. As discussed below in Section VII, competitive markets employ depreciation based upon economic lives; as a result, new technologies and innovative services are introduced (and discontinued) in a timely fashion, and network efficiencies result, all to benefit the public interest. SNET encourages the

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<sup>52</sup> SONET transmission, ATM features, and IAN platforms are examples of newer, technically advanced capabilities which can differentiate one competitor from another.

Commission to structure its guidelines in such a way as to encourage competitive deployment of new technologies to meet market needs and/or reduce costs. Any interference (including regulatory scrutiny) in the delivery of new technologies to the market would delay consumers receiving the benefits of those technologies. The Commission should only regulate *services*, not the technological platforms that deliver them.

VI. ILECS SHOULD BE PERMITTED TO RECOVER REMAINING EMBEDDED INTERSTATE COSTS (NPRM, paras. 247-270.)

A. The Commission Should Provide For Recovery Of A Deficiency In The Depreciation Reserve Caused By Under-Depreciation And Economic Obsolescence.

The Commission has undertaken an analysis of proposed treatment for any remaining embedded costs allocated to the interstate jurisdiction once access reform is implemented.<sup>53</sup> As a general matter, SNET believes that the Commission has an obligation implicit in the regulatory and social contract, if not a legal obligation, to permit ILECs a fair opportunity to recover embedded costs. This cost recovery can occur even if a reformed access regime is based upon a forward-looking (rather than historical), or a cost-causative (rather than subsidy-laden) costing approach.<sup>54</sup>

The Commission, in its review of possible proposals, acknowledges MCI's claim that, through use of the Hatfield model, the difference between accounting cost and forward-looking economic cost cannot be attributed to under-depreciation.<sup>55</sup> However, the Hatfield model methodology does not in fact define or develop economic lives to calculate economic depreciation expense. Rather, the model utilizes only nation-wide average Commission prescribed lives. These prescribed

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<sup>53</sup> NPRM, paras. 247-270.

<sup>54</sup> SNET recommends that the reserve deficiency be recovered by a discreet charge to the IXC's. See Section B. below.

<sup>55</sup> NPRM, para. 247.



lives are not, however, good estimates of economic lives. As such the costs developed by this model are not economic costs and therefore cannot be relied upon.

Under-depreciation occurs when the current net investment of ILEC assets exceeds the current economic investment using new technology.<sup>56</sup> The reason for this disparity is that historical depreciation lives had been set unrealistically long, and were not based on the current environment of rapid technology substitution, full competition, and decreasing cost and increasing efficiency of replacement technology. The result is that the book depreciation reserve is too low to reflect the current investments' true loss in economic value.

1. SNET Has Identified Its Reserve Deficiency.

The Commission acknowledges that, in a monopoly environment, there were no competitive providers and market based prices which would prevent the ILEC from eventually recovering their capital over the prescribed depreciation lives.<sup>57</sup> SNET believes that under regulation, the result of prescribing depreciation lives that were longer than economic lives was not a financial loss, but rather a postponement

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<sup>56</sup> This point is fully developed in attachments to USTA's Comments filed today in this proceeding. See "The Depreciation Shortfall," Strategic Policy Research, and "Implications of Technology Change on the Local Exchange Carriers," Technology Futures, Inc.

<sup>57</sup> NPRM, para. 250.